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PARTNERSHIP FOR ADVANCING REFORMS IN THE ECONOMY IN BOSNIA AND HERZEGOVINA

**YEAR 3 ANNUAL REPORT
MARCH 5, 2010 – MARCH 5, 2011**

April 2011

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PARTNERSHIP FOR ADVANCING REFORMS IN THE ECONOMY IN BOSNIA AND HERZEGOVINA

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Contract No. 168-C-00-08-00102-00

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The author's views expressed in this publication do not necessarily reflect the views of the United States Agency for International Development or the United States Government.

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FOREWORD

This document is the Year 3 Annual Report for the period from March 5, 2010 to March 5 2011 submitted by USAID's PARE project in Bosnia-Herzegovina.

PARE is being implemented by Chemonics International pursuant to contract No. 168-C-00-08-00102-00 that the company has executed with the U.S. Agency for International Development (USAID). This report presents the progress made during the reporting period and provides relevant information regarding the activities completed and accomplishments achieved during Year 3 of the project's operation.

PARE would also like to acknowledge the valuable guidance and support provided by USAID/PARE Contracting Officer's Technical Representative (COTR), Amira Vejzagić-Ramhorst.

Sarajevo,
April 2011

ABBREVIATIONS

ABRS	Banking Agency of RS
AMFI	Association of Microcredit Institutions
AZOBiH	Insurance Agency of BiH
BCP	Basel Core Principles
BiH	Bosnia and Herzegovina
BIS	Bank for International Settlements
BLSE	Banja Luka Stock Exchange
BSA	Banking Supervisory Agency
CBBH	Central Bank of Bosnia-Herzegovina
CBR	Committee for Banking Reforms
CMS	Credit Management System
COP	Chief of Party
COTR	Contracting Officer's Technical Representative
DCA	Development Credit Authority
DIA	Deposit Insurance Agency
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECB	European Central Bank
EU	European Union
FBA	Banking Agency of FBiH
FBiH	Federation of BiH
FSAP	Financial Sector Assessment Program
IA	Internal Audit
IAIS	International Association of Insurance Supervisors
IFC	International Finance Corporation
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IOSCO	International Organization of Securities Commissions
IRPF	International Real Property Foundation
KRA	Key Result Area
LOP	Life of Project
LPG	Loan Portfolio Guarantee
M&E	Monitoring and Evaluation
MFT	Ministry of Finance and Treasury of BiH
MRT	Market Risk Team
PARE	Partnership for Advancing Reforms in the Economy
PIFC	Public Internal Financial Control
PIR	Project intermediate result
PMP	Performance monitoring plan
PMU	Project management unit
RS	Republika Srpska
SAA	Stabilization and Association Agreement
SAI	Supreme Audit Institution
SASE	Sarajevo Stock Exchange
UBBH	Banks Association of BiH
USAID	U.S. Agency for International Development
WG	Working Groups

SECTION I. EXECUTIVE SUMMARY

USAID's Partnership for Advancing Reforms in the Economy (PARE) is a four year activity focused on assisting the government of Bosnia-Herzegovina (BiH) with financial-services sector reforms. It is designed to strengthen the regulatory framework for the financial-services sector, improve the financial administration of public resources, and improve the enabling environment for private-sector investment and growth by providing targeted, demand-driven assistance.

PARE's flexible, demand-driven approach, allows its counterparts to shift priorities and activities in order to strengthen institutional capacity and assist BiH on its path towards joining the European Union. To reach this objective, the project works through the following project intermediate results (PIRs): PIR 1: Regulatory System for the Financial Services Sector Strengthened, PIR 2: Financial Administration of Public Resources Improved and PIR 3: Enabling Environment for Financial Services Improved.

PARE's approach remains focused on providing technical assistance that: (1) increases convergence within the country and with EU, (2) has counterpart buy-in and ownership, (3) complies with the *acquis communautaire*, (4) produces meaningful, measurable results, and (5) builds donor synergies.

In Y3 PARE progressed well across all components, establishing a positive outlook for successful completion in March 2012 when the project contract ends. The project performance monitoring plan (PMP) objectives are 80 percent complete, placing the project ahead of schedule at a point 75 percent through the life of the project (LOP). The technical assistance interventions have been developed and implemented in close partnership with the key financial sector institutions and other donors. Specific technical assistance achievements and deliverables are listed below:

- Introduction of international banking supervision standards (Basel II/III) have been continued through two main avenues of project technical assistance: (i) regulatory framework strengthening and (ii) capacity building.
- Assistance to regulatory framework strengthening has advanced and will be finalized in Y4 by adopting a comprehensive Basel II/III legal framework. It has also resulted in "on the way" revisions to the banking supervision regulations, already in force.
- Assistance to capacity building complemented the regulatory strengthening by increasing partner institutions' ability to implement international standards introduced through the advanced regulatory framework. This included a US Study Tour organized for principals of BiH financial sector institutions. They benefited from the unique experience of learning about US financial regulators' responsibilities and practices.
- Private public dialogue was strengthened through closer involvement of the private banking sector in banking supervision advancement secured through the BiH Banks Association (UBBH) and its Committee for Banking Reforms (CBR).
- The BiH Deposit Insurance Agency has further consolidated and stabilized its investment policies and developed a deposit threshold and bank premium model to preserve reserve fund sustainability.
- The State Ministry of Finance and Treasury (MFT) committed itself to partner with the project on the establishment of the Financial Development Council (FDC), a

mandatory forum formed under law, for coordination of a forward looking financial policy among the key BiH financial sector institutions, including the private sector representatives. The MFT has signed a Letter of Intent (LoI) on receiving technical assistance from the project to: (i) prepare the law on the FDC (ii) increase its capacity and form a financial sector unit (FCU). In support of these activities, in the third year of the project several technical assistance (TA) interventions were designed and successfully implemented with the MFT and other relevant stakeholders.

- The Project assisted in establishing a pilot internal audit unit in the public company “Rad”. This assistance encompassed the introduction of legal and other internal audit documents required by the law. The project will share knowledge gained from this experience by distributing the documents for use as templates among other public companies.
- PARE administered an enlarged DCA portfolio as USAID and Sida signed two new DCA Loan Portfolio Guarantee Agreements with Raiffeisen Bank Bosnia and Herzegovina and Volksbank BH for 20 million USD each. The signing ceremony/press event was successfully organized by PARE on October 21, 2010.
- PARE continued TA to develop the educational content on key banking services on the BiH Central Bank web-site.
- During Year 3, the project arranged ten training programs and public events including seminars, workshops, conferences, study tours, short courses, and on-the-job trainings complimented by professional meetings which took place in BiH, the U.S. and third countries.

SECTION II. THE MACROECONOMIC ENVIRONMENT IN YEAR 3

In 2010, the economy in BiH showed signs of modest recovery after a recession caused by the global economic and financial crises, creating prospects for recovery in 2011.

The adverse impact of the economic crises in BiH was felt more in the real sector than in the financial sector, domestic demand and private investments decelerated, public spending increased sharply, and the credit boom stopped.

The negative effects of the crises, along with complex political developments, from elections in November 2010 have slowed down BiH's transition towards membership in the European Union. The country's transition has effectively been stalled and lags behind other EU candidate countries and potential candidates in south-eastern Europe.

In order to reverse negative trends and to stabilize conditions, authorities agreed on a macroeconomic program financed by the International Monetary Fund (IMF) Standby Credit Facility, to safeguard the currency board, restore fiscal imbalances and strengthen stability in the financial sector.

The macroeconomic program started to generate positive results, including fiscal consolidation, further narrowing of current account deficit, and gradual private credit growth. As a result, in 2010 the economy appears to have recovered as presented in the table below:

Selected Macroeconomic Indicators	2007 (BAM bn)	2008 (BAM bn)	2009 (BAM bn)	2010 (BAM bn)
Nominal GDP	21.6	24.6	23.9	24.7
Inflation (%)	4.9	7.4	-0.4	0.9
Trade Balance	-7.9	-9.6	-6.8	-6.5
Coverage Import/Export (%)	42.71	41.22	44.71	52.11
Current Account Deficit (% of GDP)	12.9	14.6	7.5	5.2
Foreign Currency Reserves	6.7	6.3	6.2	6.4
Sovereign Debt	3.9	4.2	5.2	6.2
Banking Sector				
Total Assets	19.5	21.0	20.9	21.1
Total Loans (net of reserves)	11.3	14.5	14.1	14.6
Total Liabilities	19.5	21.0	20.9	21.1
Citizens' Deposits	5.16	5.21	5.66	6.5
Total Turnover on Stock Exchanges in BiH	2.0	0.7	0.4	0.28

Data provided by CBBH bulletin and staff & Agency for Statistics of BiH

Due to vigilant financial policies implemented by authorities, the BiH financial sector coped well with spillover from the global crises. Regulations on debt restructuring were loosened in both Entities early in 2010, enabling debtors to restructure their obligations to commercial banks and to extend their maturities to one year.

Furthermore, in 2010 confidence in the banking sector was strengthened when the insured deposit limit was raised to KM 35,000. Confidence was further increased when an additional amount for the deposit insurance fund was secured through the European Bank for Reconstruction and Development (EBRD) Standby Credit Facility.

SECTION III. ACHIEVEMENTS BY COMPONENT

A.PIR 1: Regulatory System for Financial Services Sector Strengthened

Banking Supervision

PARE successfully supported the continued development of banking supervision in BiH, including a regulatory framework for the International Convergence of Capital Measurement and Capital Standards in BiH (Basel II Framework for BiH). This was done in active partnership with the Banking Supervisory Agencies (BSAs), CBBH, and BiH Banks Association and was based on an adopted country-wide strategy and Action Plan for implementation of the Basel II Framework for BiH. This activity was also completed through the inter-agency working groups (WG) for Basel II framework implementation in BiH.

Objective

- Achieve compliance with international principles (Basel II and III, FSF, IOSCO, FSAP, EU Directives) and the implementation of ECB and OECD recommendations to achieve alignment with international and EU standards and best practices.
- Contribute to convergence and effective consolidation of banking supervision at the state level.

In Y3 the TA extended through the project has focused on two main areas: (1) strengthening of banking supervision regulatory framework based on Basel II /III standards; and (2) capacity building of institutions to complement regulatory reforms. The project has involved the banking private sector in both of these initiatives to allow for a permanent dialogue between regulators and banks, which is necessary for the successful implementation of risk-based supervision.

Also, in the Y3, the BiH financial regulators benefited from PARE technical assistance to improve the present banking supervision regulations and to create an easy transition towards the adoption of a comprehensive Basel II/III banking supervision framework, which is planned for the project Y4. These revisions are summarized in the box below. Also, these regulatory improvements empowered the BiH financial regulators to decisively respond to the financial crises challenges and to better safeguard the integrity of the financial services system.

Regulatory Adoption Achievements of PARE Y3 Assistance in Banking Supervision

(Published in the Official Gazette throughout 2010)

PARE technical assistance, capacity building, and dialogue through working groups lead to the adoption in Y3 of the following essential amendments to the existing regulatory framework by both entities' BSAs.

- Decree on Minimum Standards of Managing the Capital (own funds)
- Decree on Minimum Standards for Management of Credit Risk
- Decree on Minimum Standards for Management of Operational Risk
- Decree on Minimum Standards for Management of Market Risks
- Changes in Reporting Forms

In addition to key adoptions noted in the text box above, the details on PARE Y3 achievements and activities in banking supervision are listed below:

Own Funds and Credit Risk Decree

During Y3 PARE and the WG advanced drafts of regulations in the area of Credit Risk and Own Funds. This is of particular importance due to recent guidance issued by the Bank for International Settlements (BIS) and the Financial Stability Board with regard to capital structure, leverage ratios, and liquidity management. In February 2011 the Credit Risk Decree and Own Funds Decree were finalized, based on assistance provided from PARE from mid 2010. In addition, the BIS issued guidance regarding future capital requirements for major banks which has been taken into account while drafting Own Funds legislation.

Market Risk Team Activities

As part of USAID's ongoing technical assistance to BiH financial sector regulators, PARE facilitated the formation of the Market Risk Team (MRT) comprised of representatives from the CBBH and the entity-level BSAs. The group is the first risk-based supervisory team formed and is charged with leading the development and supervision of all market and liquidity risk oversight methodologies on a bank-by-bank basis. The MRT held three sessions, in April, July and December of 2010. The MRT has been working on specific tasks related to development and supervision of market risk processes on an individual bank basis.

Market Risks Decree

The MRT was presented with final draft decree on Market Risks aligned with CRD2 and CRD3 newly adopted solutions. During a three-day PARE organized study-tour in Slovenia members of the team had the opportunity to acquire best practices in supervising these risks by studying the case of the Bank of Slovenia and Slovenian commercial banks. This hands-on training provided by Center for Excellence in Finance (CEF) was of the cornerstones to efforts in capacity building during Y3.

Recent developments of EU regulatory framework

PARE TA has provided the counterparts with information on the latest developments in the EU regulations and bank supervision. To that end the "Banking Supervision Reforms - EU Directives and Risk Management" seminar was held in Sarajevo on September 3, 2010. The workshop gathered over 50 participants representing the banking supervision organizations in BiH, banking industry as well as all key regulatory and supervisory institutions in the BiH's financial sector.

US Study Tour for Financial Regulators

PARE organized a Study tour to the U.S. for the BiH financial regulators and supervisors to provide them with the opportunity to learn about regulatory changes and improvements in the financial system of a leading world economy. The delegation included senior-level officials from banking agencies of the Federation of BiH and Republika Srpska (the RS), the CBBH, the Deposit Insurance Agency of BiH, and the Insurance Agency of BiH, while visiting Washington, D.C., and New York City. The study tour was considered a success by its participants.

In addition to providing general exposure to U.S. financial sector regulation and oversight, the program included visits to key U.S. institutions, including the Federal Deposit Insurance Corporation (FDIC), the Financial Industry Regulatory Authority (FINRA), the

Securities Industry and Financial Markets Association (SIFMA), and the U.S. Treasury. Particular attention was paid to the future architecture of the global financial system and the new framework of regulation and supervision to help maintain financial stability.

Participants perceived the exchange of information and identification of new trends in the regulatory structure of US financial institutions as valuable experiences to apply to regulatory strengthening of BiH institutions for EU accession. (A full Study Tour Report is in Annex 4)

Committee for Banking Reforms established by BiH Banks Association (UBBH)

In order to strengthen a public private dialogue formalized in the Letter of Intent (LoI) signed between PARE and Banking Association of Bosnia and Herzegovina at the end of Y2 of the project, UBBH had established the Committee for Banking Reforms. It is composed of representatives of six banks in BiH and members hold positions either on managing boards of their respective banks or as chief risk officers. The committee has participated in the key TA interventions extended to banking supervision.

Impact Analysis of BiH Banks

As a compliment to banking supervision TA, PARE also engaged a local consultant to prepare an impact analysis of the current institutional and human resources, and infrastructure preparedness of ten BiH banks (with/without connections to EU banks) for implementation of new risk based regulatory framework. The outcomes of research will be presented to both regulators and the private sector explaining the impact of the proposed regulation on the capital and financial standing of small and medium BiH banks.

Glossary of Financial Terms

Through its technical assistance activities the PARE team continued to collect specific professional terms into a glossary. To date, more than 95 items related to banking supervision, risk management, market risks, deposit insurance scheme, financial planning, and other topics have been collected. This is a work in progress and will be continued in Y4.

Basel II Website

The Basel II website was created for use by PARE and working groups implementing the Basel II Framework (www.bankarska-supervizija.info). The Basel II website has been maintained to store all relevant information about the reform processes as well as the activities of the working groups. The website was developed following the Committee of European Banking Supervisors (CEBS) standardized format. The website is used to share key documents between the working group members and key stakeholders. The content of the website is composed of reports prepared by consultants and information about activities of the working groups.

Deposit Insurance Agency

PARE and the DIA developed an integrated model for financial planning to (i) determine the eligible insured deposits threshold (coverage), (ii) assess the required size of the Reserve Fund, and (iii) define the level of insured deposit premiums. This model enables the DIA staff to regularly examine the situation in the banking

Objective

- To help the DIA revise its investment policy and guidelines to incorporate EU member states' practices and to update the model for eligible insured deposit thresholds.

sector and determine corresponding premiums to ensure adequate coverage of the Reserve Fund.

The model is an excellent tool to support the policy decision making process. It serves to assess the Fund's exposure and determines the level of deposit insurance premiums in light of the recent increase of the deposit insurance limit to KM 35,000, (as well as an expected increase to KM 50,000) and inclusion of legal entities' deposit into the deposit insurance scheme. Following the completion of the model development, PARE organized a workshop for the DIA staff for training in the new model and to ensure the sustainability of the DIA's continuous administration and use of the model, including updates.

PARE has continued to assist with strengthening the policy framework for DIA's investment management activities, resulting in a sustainable and liquid DIA Reserve Fund. PARE continued delivering capacity building to the DIA staff to effectively implement and monitor its investment policies. During Y3, the project worked directly with the DIA and members of the Investment Committee to review and update the implementation of the Investment Guidelines and the Investment Policy Statement that were previously developed under PARE assistance.

Insurance Supervision

In Year 3, the FBiH Insurance Supervision Agency requested PARE to assist with the introduction of a system of risk-based supervision and the establishment of an overall statistical reporting system. The details of the request were specified in the letter submitted to PARE in August, 2010.

Objective

- To help bring the insurance sector closer to effective consolidation and the insurance supervision agencies to become independent regulators thereby moving BiH closer to a single economic space.

Based on this request, PARE has held several technical meetings with insurance agencies in order to better understand the context of the technical assistance request. A lack of insurance statistics has been identified by both BiH institutions and international financial institutions as one of the major gaps in the insurance sector. The insurance agencies intend to establish a common platform for statistical reporting in accordance with Solvency 3, Eurostat requirements and other applicable international standards. The insurance agencies in BiH also need their capacities strengthened to perform offsite supervisory functions and to facilitate data/information flows, the latter in order to produce adequate insurance sector statistics.

The insurance sector data flow system should originate from insurance companies, through the entity-level supervisory agencies, to the State-level insurance agency, and onward to EUROSTAT and the CBBH. Facilitating the first step in this direction, PARE helped to make a review of the existing software and hardware capacities of insurance agencies ("As-Is" and "Gap-Fit" Analysis). The analysis indicated that Insurance Agency of BiH and Insurance Supervision Agency of FBiH may need to make further investments in both hardware and software to advance their operations.

Institutional Coordination between Stakeholders within Financial Sector Strengthened (Track 2)

In Year 3, PARE has continued its activities to improve financial sector convergence and institutional coordination as BiH financial system institutions remain fragmented with

weak coordination and with no opportunity to formulate common, progressive policies. The private financial sector is also missing a single partner to address its needs for the creation of a functional and enabling business environment which would be comparable to that of developed countries. The project has therefore proposed the establishment of BiH Financial Development Council (FDC) with the MFT as a champion. The MFT committed itself to technical assistance by signing a Letter of Intent (LoI) to formalize cooperation with PARE. FDC members include representatives of entity and state level ministries of finance, supervisory and regulatory agencies, and representatives of the private sector. The MFT will support the work of the FDC through the Financial Coordination Unit (FCU) within the MFT, which will also serve as the technical secretariat for the FDC. The process of establishing the FDC is a highly sensitive political topic and will depend on further political developments in 2011.

A concept paper and a draft law on the FDC were prepared and discussed with relevant experts and counterparts. PARE organized a series of meetings regarding the FDC, engaging the Minister of Finance and Treasury of BiH (MFT), Assistant Ministers and technical experts, private sector associations of leasing and insurance companies, as well as USAID/BiH Mission, to obtain their feedback.

The MFT has reconfirmed its commitment by signing, on September 7, 2010, a LoI with the project. Based on the LoI, PARE is providing support to the MFT to establish a Financial Coordination Unit (FCU). The MFT identified potential personnel for the FCU and asked the Project to help with the selection and screening process. In January 2011, PARE developed an inception report for MFT and FCU capacity building, suggesting the use of the FCU, providing a preliminary outline of the FCU training needs, and specifying a detailed capacity building action plan and other items necessary for efficient establishment of the FCU.

In March 2011, the Minister of Finance appointed six members to the FCU, consisting of the MFT professional staff (financial sector experts, macroeconomists and researchers). The continuation of technical assistance from PARE will include capacity building activities (specified in the inception report) and activities on advancing FDC Law.

B.PIR 2: Financial Administration of Public Resources Improved

Pilot Internal Controls and Audit Units Established

In Y3, PARE planned to offer TA to a pilot internal audit unit at public enterprises or government institutions. In early 2010, PARE identified the city of Banja Luka as a potential candidate, but due to internal complexities in the Banja Luka City Administration, the project decided not to proceed with this assistance.

PARE's technical assistance in this area has been coordinated with the EU-funded twinning project for public audit system harmonization (Introducing Central Harmonization Units CHU), which was officially launched in May 2010. In order to avoid overlapping with EU assistance to government institutions, PARE chose to work instead with public enterprises.

PARE selected the public utility company Rad Sarajevo (Rad) for the first pilot internal audit unit. On June 14, 2010, Rad submitted a letter of commitment, expressing interest in working with PARE on establishing an internal audit pilot unit.

PARE assisted Rad's IA unit in introducing international and advanced practices in its internal audit operations. In addition, PARE worked with Rad's IA unit to develop a set of documents, including a risk assessment framework, risk-based strategic and annual audit plan, standardized IA templates, such as an audit report with recommendations, quarterly and annual reports, and standardized legal and other documents required by law and other applicable provisions. These documents are important tools for the IA unit to increase IA capacity and improve internal audit functions.

This IA pilot unit will serve as a model unit and the IA set of documents/reports can easily be replicated in other similar public enterprises as well as institutions and agencies in BiH and IA functions within public institutions.

The document templates that PARE developed during the provision of TA to "Rad", including a risk register, a risk assessment, and periodic IA reports, will be disseminated at the Internal Audit Round Table in May 2011.

C.PIR 3: Enabling Environment for Private Sector Investment Improved

PARE TA interventions under PIR 3 have been reflected through improvements to the business environment for those who supervise or use financial services in BiH.

The project explored an opportunity to provide TA to Appraiser's Professional Associations, as appraisal professional services are a key component to risk mitigation, and therefore remain an important element of risk based supervision reforms assisted by the project.

Objective

- To develop modern and effective financial intermediation and strengthen associations of financial professionals.

PARE assisted in the preparation of an assessment which indicated that the Association of Accountants and Auditors of the RS (RSAAA) may have the ability to provide professional services in line with international valuation standards (IVS). Also, the Accounting and Auditing Committee of BiH (AACBH) supported the idea to have nationwide recognition of certificates, and the Association of Accountants, Auditors and Financial Professionals of FBiH (FAAA) approved the activity. The three parties sent a letter to PARE requesting specific technical assistance to align existing curriculums and certification processes with the IVS 2007. However, the project had to prioritize TA activities and was unable to include this TA demand among them.

Moreover, PARE TA interventions realized under PIR 1 have impacted financial intermediation positively and improved over business environment in BiH.

D. Srebrenica component (expired on September 1st, 2010)

The Srebrenica Business activity was originally managed by the USAID-Funded Streamlining Permits and Inspection Regimes Project (SPIRA), upon this project's closure in 2009, the activity was transferred to PARE where it was managed to completion in September 2010.

Objective

- To attract investment and improve the local business environment.
- To develop the municipal economic department's capacity.

The following key initiatives and accomplishments took place under this activity:

- An economic development training trip for Srebrenica municipal leaders to Koprivnica and Varazdin, Croatia, was completed. Participants were exposed to progressive trends in public-private partnerships and regional, rural, and local economic development.
- The municipal Unit for Integrated Development was formally established in July of 2010. Their key tasks are to apply EU IPA facts and deal with investment attraction and other activities.
- Specialized training activities took place in the areas of rural and local economic development, rural entrepreneurship, and promotion and branding of local products. In total, seven courses were delivered over sixteen days to a daily audience varying between six and twelve participants, including those from local NGOs.
- In addition, the Srebrenica component coordinated activities with the FARMA project – specifically supporting new local dairy producers in Skelani as well as other local agricultural producers.

E. USAID Development Credit Authority (DCA) Loan Portfolio Guarantee (LPG) Facility

During the reporting period, the following DCA activities/requirements were realized:

- Semi-Annual Loan Schedule Reports (March 2010 and September 2010) were completed through USAID's Internet-based Credit Management System by the two BiH DCA LPG partner banks (Volksbank BH and UniCredit Bank). The status of the DCA LPG facility in BiH, including data for the Intesa Sanpaolo Bank BiH, is presented below in the table "DCA LPG Summary as of September 30, 2010."
- The Annual Certification of Post-Claim Recoveries (Certifications for Net Recoveries and the Schedules of Net Recoveries) was completed and submitted to the USAID/Washington, Office of Development Credit, by the designated deadline (July 30, 2010). All three BiH DCA partner banks certified that there were no recoveries received subsequent to the Claims paid by USAID.
- DCA Checklist Forms on DCA Portfolio Environmental Changes and Environmental Policy Changes dated April 15, 2010, July 15, 2010, October 19, 2010, and January 20 2011, were fulfilled with UniCredit Bank. The Bank reported that the Bank's Management Board approved a new Environmental Protection Procedure on January 18, 2010, and then on May 24, 2010, after the improvement of the document (per IFC request) and change of the name (Procedures Environmental Protection, Social and Health Security and Community Safety).
- In June 2010 a representative of USAID Office of Development Credit from Washington, Mr. Reid W. Click (senior Credit Analyst), conducted audits in two banks (Raiffeisen Bank BiH and VolksbankBH) selected for a new joint USAID/Sida loan guarantee program in BiH. Mr Reid also visited other institutions (including Federal Banking Agency, USAID/Sida-funded projects FIRMA and FARMA, and DCA Volksbank wood processing company RAMEX in Kladanj) with representatives of USAID Sarajevo (Amira Vejzagic-Ramhorst) and PARE (Muhiba Adanalic).
- Three Requests for Payment of Claim (from the companies Biovita from Mostar, Mega Komerc from Novi Grad, and Zemljoradnicka Zadruga from Fojnica) submitted by Volksbank BH (one) and UniCredit Bank (two), were analyzed, and memorandums on the approvability of these requests were prepared and delivered to USAID Sarajevo on August 17, 2010, November 4, 2010 and November 12, 2010, respectively. Volksbank's Claim Request for the company Biovita was paid by USAID on October 18, 2010.
- One Request for DCA Coverage (an exception for a loan made in connection with refinancing, repayment or repurchase of an existing loan) submitted by the Volksbank BH (company Limprodukt from Kresevo) was analyzed and a memorandum on the approvability of this request was delivered to USAID on December 10, 2010, along with comments and recommendations prepared by the FIRMA Metal Processing (MP) Sector specialist.
- On September 20, 2010, USAID and UniCredit Bank, a legal successor of the UniCredit Zagrebacka Bank, signed an Amendment to the DCA Guarantee Agreement

No. DCA-LPG-168-06-005 to extend the Final Date for Placing Qualifying Loans under Coverage from 4 to 9 years from the date of the Agreement (September 2006). All other provisions/terms/conditions of the Agreement remained in full force and effect.

- On September 20 and September 24, 2010, USAID and Sida signed two new DCA Loan Portfolio Guarantee Agreements with Raiffeisen, Bank Bosna and Herzegovina, and Volksbank BH of 20 million USD each. The signing Ceremony and press event was organized by PARE on October 21, 2010.
(Annex 4, DCA Loan Guarantee Program Signing Ceremony)
- A Fact Sheet on DCA facility in Bosnia and Herzegovina was developed (Annex 6).
- A Presentation on the BiH DCA facility was prepared by PARE specialist Muhiba Adanalic and presented at the Program for Business Finance Consultants (November 2010) and symposium on Access to Finance (February 2011) organized by USAID/Sida FIRMA project.
- The PARE DCA specialist organized a few coordination meetings with the representatives of USAID /Sida projects FIRMA and FARMA and representatives of DCA partner banks (Raiffeisen Bank BiH, Volksbank BH and UniCredit Bank) to discuss possibilities of joint activities for the successful utilization of the DCA LPG guarantees.

DCA LPG Summary as of September 30, 2010

	TOTAL	(%)	UPI / Intesa Sanpaolo Bank BiH	Volksbank BH	Zagrebačka / UniCredit Bank	
Guarantees						
Number			168-03-001	168-03-003	168-03-002	168-06-005
Start Date			2003/07/08	2003/08/07	2003/08/27	2006/09/30
End Date			2010/07/08	2010/08/07	2010/08/27	2016/09/29
Portfolio (# loans)						
# Allowed Loans	205	100%	82	39	52	32
Agriculture	119	58%	43	27	36	13
Wood industry	68	33%	39	11	6	12
Tourism	18	9%	-	1	10	7
# Loans subject to claims	15	7%	9	4	1	1
Loans						(US \$ million)
Approved	47,00	100%	10,00	12,00	9,00	16,00
Used	30,88	66%	7,62	10,56	8,71	3,99
Available	12,01	25%	-	-	-	12,01
Expired	4,11	9%	2,38	1,44	0,29	-
Ending Balance	4,96		-	1,74	0,87	2,35
Total in Arrears	1,62		-	1,21	0,41	0
Claims						(US \$ million)
Total	1,40		0,96	0,29	0,12	0,03
Paid	1,40	100%	0,96	0,29	0,12	0,03
Pending	-	-	-	-	-	-
Employment Summary						
Current Employment	2832		1357	484	628	363
Planned Employment	601		54	269	188	90
Fees Summary						
Total Fees paid (US \$)	US \$ 231,336		US \$ 32,850	US \$ 96,321	US \$ 68,110	US \$ 34,055
Loan details Summary						
Average Loan Size (US \$)			US \$ 88,332	US \$ 256,521	US \$ 171,056	US \$ 138,247
Average Tenure (Days)			382 Days	1790 Days	1641 Days	1713 Days

Portfolio at Risk						
# Active Loans	58	100%	-	17	13	28
Total # Loans in Arrears (1+ Days)	13	22..4%	-	8	5	0
Percent of Portfolio in Arrears (1+Days)			-	69.88%	47.78%	0%
# Loans in Arrears (91+ Days)	7	12.0%	-	2	5	0
Percent of Portfolio in Arrears (91+Days)			-	28.50%	47.78%	0 %

Note: **Percent of Portfolio in Arrears (1+Days) = Total Portfolio in Arrears / Ending Balance**

F. Training Activity

During Year 3, PARE arranged ten training programs and public events, including seminars, workshops, conferences, study tours, short courses, and on-the-job trainings complimented by professional meetings, which took place in BiH, the U.S., and third countries. These training activities supplemented the project's TA, which supports project counterparts in strengthening the regulatory system for financial services, improves the financial administration of public resources, and enhances the environment for private sector investments. The topics of training activities included banking supervision, deposit insurance, financial regulation and oversight, insurance supervision, strengthening internal audit functions, and other related subjects. Below is the list of training activities and public events organized during the reporting period.

1. Market Risk Team Formation (April 20, 2010, Jahorina, BiH);
2. Financial Model for Calculation of Deposit Insurance Premiums (April 27, 2010, Mostar, BiH);
3. Market Risk Work Team Session II (July 7- 8, 2010, Teslić, BiH);
4. Banking Supervision Reforms-EU Directives and Risk Management (September 3, 2010, Sarajevo, BiH);
5. Letter of Intent between PARE and the Ministry of Finance and Treasury of BiH Signing Ceremony (September 7, 2010, Sarajevo, BiH);
6. Preparation of Internal Audit Risk Assessment and Internal Audit Strategic Plan Transparency and Democracy-Role and Importance of Supreme Audit Institutions On-the-job Training (September 27-29, 2010);
7. DCA Loan Guarantee Program Signing Ceremony (October 21, 2010, Sarajevo, BiH);
8. Banking Supervision Coordination Meeting (October 21, 2010, Sarajevo, BiH);
9. Banking Supervision Reforms-Market Risks Decree Study Tour (December 13-17, 2010, Ljubljana, Slovenia);
10. US-based Study Tour for BiH Financial Regulators (February 5-16, 2010, Washington, DC and New York, NY);

A brief summary of the goals and objectives for each training activity organized by the project can be found in Annex 5.

G. Other Program Activities

Project Web-site

The project web site continues to provide a high level of project visibility and to inform the broader public of progress within the three project components, including the implementation of training sessions. Additionally, the PARE website has sections containing press coverage and a photo gallery that includes reports from various media outlets about project trainings/events. The project web site address is www.usaidpare.ba.

Web-base Educational Component

During Y3, PARE continued to work with CBBH consultants to develop educational components on key banking services, including savings accounts, current accounts, credit cards, investments, loans, and electronic services.

The technical information on banking services included in the website will also help to clarify advantages and disadvantages of the various services and products offered by banks to individual consumers, including savings and current accounts, loans, and credit

cards, among others. The continuous financial and economic education of PARE's target audience is a pre-condition for successful implementation of the project's activities and reforms. The web-based education components are accessible at www.cbbh.ba.

H. PARE's Participation at Select Major Events

Europe & Eurasia Bureau 5th Annual Regional Event on Competitiveness, Finance and Economic Growth, May 18 – 20, 2010

From May 18-20, 2010, PARE Chief of Party (CoP) Berina Selimovic-Mehmedbasic took part in the 5th Annual –Conference "Competitiveness, Finance and Economic Growth", organized by USAID Europe and Eurasia Bureau's Economic Growth Office (EE/EG) in Sarajevo. The EE/EG Regional Competitiveness Initiative (RCI) included regional stakeholders from South East and Eastern Europe and the Caucasus, and featured local and international experts. Participants shared best practices, success stories, lessons learned, future opportunities for cooperation, and USAID project experience in the region.

During the PARE related presentation of the Bosnian Government's Response to the Global Financial Crisis, Mrs. Selimovic-Mehmedbasic spoke about the structure and characteristics of the BiH government and financial sector, the BiH economy before the financial crisis, and how the crises has impacted the BiH financial sector (<http://www.rciproject.com/rcibhpowerpoints1.html>).

The Deputy Assistant Administrator (DAA), Europe & Eurasia Bureau, Jonathan Hale visited Bosnia and Herzegovina, June 1-5, 2010

On June 4, 2010, PARE organized for the DAA to meet with the DIA in Banja Luka. During the meeting the DAA learned about the valuable assistance previously provided by USAID and currently provided through PARE. The DIA management acknowledged the significant technical assistance DIA received from PARE over the last two years, which helped the DIA to maintain sound and stable functions.

Committee for Coordination of Banking Supervision of CBBH, FBA and BARS meeting on June 30, 2010

On June 30, 2010, PARE presented the progress of banking supervision reforms to members of the Coordination Committee, including the Governor and Vice-Governors of the Central Bank of BiH, Directors and Deputy Directors of the banking supervision agencies, and the Deposit Insurance Agency. The presentation described the structure and approach to the banking supervision reforms, plan of activities, accomplishments to date, next steps, and presented the working groups' requirements for senior management of these institutions.

Financial Services (FS) Practice Event, June 10, 2010

On June 10, 2010, PARE COP Berina Selimovic-Mehmedbasic took part in the 1st Virtual Chief of Party (COP) Conference organized by the Financial Service (FS) Practice for all FS Chemonics COPs. Participants shared information on project innovations, challenges, and FS project updates. During the PARE related presentation, Mrs. Selimovic-

Mehmedbasic spoke about project innovations and challenges and presented a newly created Basel II Website Portal as an interactive tool for banking supervision reforms.

Banks Association of BiH Annual Meeting, November 19, 2010

The PARE team participated in the Annual Meeting of the Banking Association of BiH (UBBH). The meeting's participants included the vice-governor of Central Bank, directors of the Banking Agencies, and representatives of the entity-level ministries of finance, tax authorities, and SIPA's Financial Intelligence Unit, as well as the senior managers of all BiH banks.

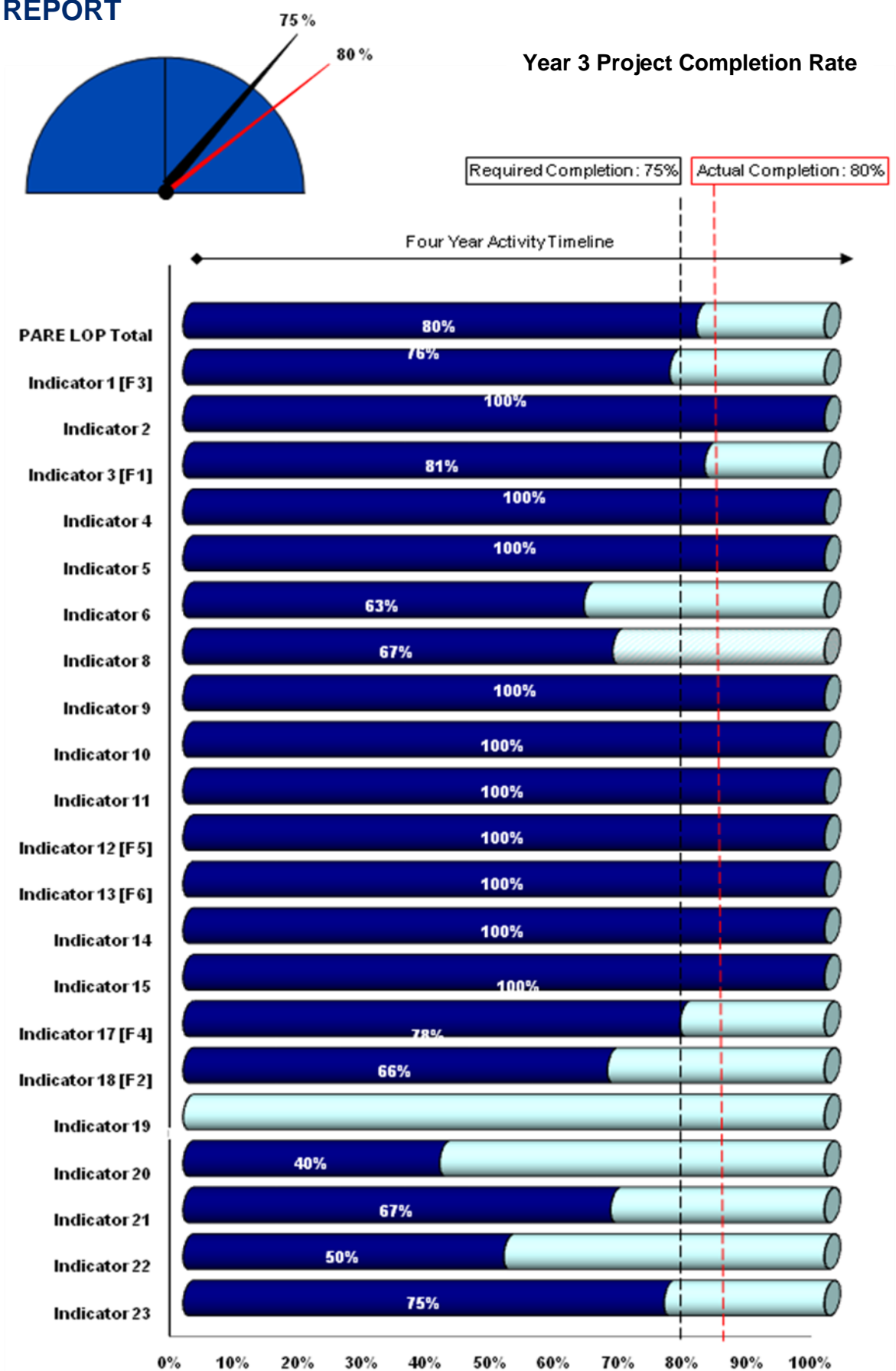
The discussed topics included the macroeconomic outlook for BiH; banking industry outlook in 2011; consumer protection in the banking industry; novelties in anti money-laundering (AML) regulations in BiH; and improvements on financial foreclosures.

Participation of the PARE team was welcomed and recognized as an important contribution.

Other Selected Events

- Inauguration Event – EU Twinning Project Support for Sustainable Capacity Building of the Insurance Agency of BiH and the F BiH and RS Insurance Supervisory Agencies, May 2010
- Round Table on Consumer Protection in the Banking Sector, June 2010.
- Banking Excellent Awards (BAM) by Banka Magazine, Ceremony, June 2010
- Round Table on BiH Microcredit Sector Reform and Legal Framework, July 2010.
- Round Table with banks in BiH on the “Challenges of Financing Energy Efficiency Projects” organized by USAID 3E project - September 2010
- Conference on “The Future of Public Financial Management Reform in BiH” organized by Department for International Development (DFID) - September 2010
- Committee for Coordination of Banking Supervision of CBBH, FBA and BARS meeting - October 2010
- The Sarajevo Stock Exchange (SASE) Conference on “The Capital Investments and the Capital Markets” - October 2010.

SECTION IV. CONSOLIDATED PERFORMANCE MANAGEMENT REPORT



PARE's activities, performance, and progress were measured on the basis of the Project Performance Monitoring Plan (PMP), actual for Y3 versus the Y3 target and actual Project Start to Date (PSD) and compared to the 4 Year Life of Project (LOP) plan.

No.	Indicator	(1) Y3 Result	(2) Y3 Target	(3) Y3 Rate	(4) PSD Result	(5) LOP Target	(6) PSD Rate
	Explanation			(1)/(2)			(4)/(5)
1	Number of internationally recognized financial-sector standards adopted as a result of USG assistance (F Indicator 3)	2.33	2.5	93%	6.83	9	76%
2	Level of counterpart satisfaction with the quality of the technical assistance and deliverables	4.88	4	122%	4.76	4	119%
3	Number of financial-sector supervisors trained with USG assistance (F Indicator 1)	123	160	77%	449	552	81%
4	Progress toward banking supervision framework that promotes effective consolidation at the state level (milestones)	6	6	100%	6	6	100%
5	Percentage of inspections and directives issued that are compliant with current laws	-	-	-	100%	100%	100%
6	Progress toward IAIS-based insurance supervision framework that contributes to consolidation of economic space for the insurance sector (milestones)	0.5	2	25%	2.5	4	63%
7	Progress toward establishing a fixed income securities market with appropriate supervision and oversight (milestones)	/	/	n/a	/	/	n/a
8	Progress toward reform of targeted leasing and factoring policy or regulation (milestones)	-	-	-	2	3	67%
9	Number of steps achieved toward a revised DIA investment strategy that incorporates EU best practices	7	7	100%	7	7	100%
10	Updated model regarding eligible deposit threshold incorporating considerations of EU standards developed and implemented	1	1	100%	1	1	100%
11	Number of by-laws (rulebooks, guidelines, etc) developed with project assistance in Private Pension Fund	-	-	-	5	2	250%
12	Number of national executive oversight actions taken by legislature receiving USG assistance (F Indicator 5)	-	-	-	63	61	103%
13	Number of mechanisms for external oversight of public resources supported by USG assistance and implemented (F Indicator 6)	-	-	-	14	12	117%
14	Number of media and public awareness events about SAIs' reports, audit findings, recommendations, and proceedings held	-	-	-	121	58	208%
15	Number of pilot internal audit departments established in governments and/or public enterprises	1	1	100%	1	1	100%
16	Number of certification programs for financial sector professionals offered by professional as a result of project assistance	/	0	n/a	/	0	n/a
17	Number of national legislators and national legislative staff attending USG-sponsored training or educational events (F Indicator 4)	8	12	67%	62	80	78%
18	Number of financial-sector professionals trained on international standards this year with USG assistance (F Indicator 2)	96	109	88%	217	328	66%
19	Progress toward mapping legislation to determine legal impact of Basel II implementation (milestones)	0	2	0%	0	3	0%
20	Glossary of Financial Terms developed (yes/no)			40%			40%

No.	Indicator	(1) Y3 Result	(2) Y3 Target	(3) Y3 Rate	(4) PSD Result	(5) LOP Target	(6) PSD Rate
21	Progress toward private sector engagement in banking supervision reforms through UBBH	2	2	100%	2	3	67%
22	Progress toward establishment of Banking Supervision Council (BSC)/Financial Development Council	2	3	67%	2	4	50%
23	Progress toward building capacity of the BiH Ministry of Finance and Treasury (milestones)	3	3	100%	3	4	75%

SECTION V. ADMINISTRATION AND PROJECT MANAGEMENT

To implement its demand-driven approach and broad scope of work, PARE's core team of long-term technical staff, operated between the Sarajevo and Banja Luka offices to facilitate communication and build relationships with counterparts and partners countrywide. This core team is complemented by short-term technical assistance from local and international specialists who provide a range of specific technical expertise in a targeted and cost-efficient manner. The project field office team is supported by a project management unit (PMU) in Chemonics' home office.

PARE COP Berina Selimović-Mehmedbašić manages overall implementation of project activities, relationship-building with counterparts, and the monitoring of project results. Each member of the core team is assigned two or three specific activities across project components to ensure accountability and consistency for each results area. Component 1 activities are divided among Dario Vins (financial sector specialist), Slavisa Raković (economic specialist), Amil Kamenica (financial sector associate). In addition, Muhiba Adanalić, the DCA/M&E specialist, manages USAID's DCA portfolio and works with the core team to monitor project performance against the established indicators. Amra Softić (communications and training specialist) focuses primarily on administration of training and communication activities. Boris Maslo (lawyer associate) left the project in May 2010 to get a position of a Chief of Party with the USAID Government Accountability Project (GAP). The office manager/accountant, Sanin Muftić, oversees the operations of this team with the assistance of Svetlana Prastalo. The administrative staff is responsible for the project's administrative, logistical, accounting, and compliance functions.

With PARE's broad scope and specialized needs, short-term consultants are important resources. These consultants provide expert assistance to help effectively implement the project's objectives with the project counterparts. To provide consistency, in some cases PARE has identified expatriate and local short-term consultants who can provide intermittent technical assistance in their relevant areas of expertise. This support, from a variety of experts, helps the project to maintain the momentum necessary to achieve results in an extremely broad range of financial services technical areas. The PMU maintains a roster of highly qualified local and expatriate consultants who can provide targeted technical assistance in an extensive range of technical areas.

The project is backstopped by the home-office PMU, which assists with recruiting and fielding short-term specialists, budgeting, technical/contractual reporting, contract compliance, and administrative and technical support. The PMU provides support to the field to navigate USAID regulations and comply with reporting expectations.

SECTION VII. ANNEXES

Annex 1 - Detailed PMP

Annex 2 - List of Counterparts

Annex 3 - Case Studies/Success Stories

Annex 4 - US Study Tour Report -Excerpt

Annex 5 - Training Activity Blurbs

Annex 6 - DCA Fact Sheet

ANNEX 1 – DETAILED PMP REPORT

Indicator 1: Number of internationally recognized financial sector standards adopted as a result of USG assistance

Results Summary

Y3 Result	2.33	Y3 Target	2.5	LOP Target	9
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Explanation	Own Funds	Trading Standards	Risk Management	ICCAP	Liquidity
Strategy		1	1	1	1
Action Plan		1	1	1	1
2009/2010 Plan		1	1	0	0
Theoretical Preparation	1	0	1	0	0
Technical Work	1	0	0	0	0
Draft of Decision	1	0	0	0	0
Completed	50%	50%	67%	33%	33%
Y3 Rate			93%		

Indicator 2: Level of counterpart satisfaction with the quality of the technical assistance and of deliverables (satisfaction is rates from 1-5)

Results Summary

Y3 Result	4.88	Y3 Target	4	LOP Target	4
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The indicator on counterpart satisfaction was calculated using the submitted evaluations on:

- Workshop on Financial Calculation of Deposit Insurance Premiums dated April 27, 2010 (Qualitative indicator = 4.97)
- Workshop on Market Risk (Market Team-Session II) dated July 7-8, 2010 (Qualitative indicator = 5.00)
- Job training on Risk Assessment, RAD company dated September 27-29, 2010 (Qualitative indicator = 5.00)
- Seminar on Market Risk Decree dated December 13-17, 2010 (Qualitative indicator = 4.73)
- Study Tour to Washington/New York dated February 5-16, 2011 (Qualitative indicator = 4.69)

Indicator 3 (F Indicator 1): Number of financial-sector supervisors trained with USG assistance

Results Summary

Y3 Result	123	Y3 Target	160	LOP Target	552
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In total 123 supervisors attended the following workshops, seminars and technical meetings organized by the PARE project:

Workshops

- Market Risk Team Formation - April 20, 2010
- Financial Calculation of Deposit Insurance Premiums - April 27, 2010
- Market Risk Team-session II - July 7-8, 2010
- Risk Management - September 3, 2010

Technical Meetings

- Basel II Credit Risk - May 26-27, 2010

- Basel II - September 23, 2010 (Sarajevo) and October 20-21, 2010 (Banja Luka)
Seminars
- DIA model for Financial Calculation of Deposit Insurance Premiums - November 8-10, 2010.
- Market Risk Decree-December 13-17, 2010
Study Tours
- Strengthening Financial Regulation, Washington/New York-February 5-16, 2011

The Participants included 52 men and 71 women from the following institutions:

- 91 from entity BSAs
- 14 from DIA
- 17 from CBBH
- 1 from Insurance Agency of BiH

Indicator 4: Progress¹ toward banking supervision framework that promotes effective consolidation at the State level

Results Summary

Y3 Result	6	Y3 Target	6	LOP Target	6
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Implementation stage continued according to the Action/Implementation Plans

Indicator 6: Progress² toward IAIS-based insurance supervision framework that contributes to consolidation of economic space for the insurance sector (milestone)

Results Summary

Y3 Result	0.5	Y3 Target	2	LOP Target	4
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PARE had assessed the existing software and hardware capacities in all three insurance agencies in BiH (entity and state level). The assessment of IT capacities was the first step/part in the identification of appropriate statistical reporting system (milestone 4)

Indicator 9 : Number of steps achieved toward a revised DIA investment strategy that incorporates EU best practices

Results Summary

Y3 Result	7 ³	Y3 Target	7	LOP Target	7
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Follow up on the implementation of the Investment Guidelines, the Investment Policy Statement and review of the DB Asset Manager's report was realized in October 2010

Indicator 10 : Updated model regarding eligible deposit threshold incorporating considerations of EU standards developed and implemented (yes/no)

Results Summary

Y3 Result	1	Y3 Target	1	LOP Target	1
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¹ Progress is measured by the following milestones: (1) assessment, (2) strategy draft/proposal, (3) action plan approval/adoption, (4) working group(s) established, (5) implementation plan made, and (6) implementation stage.

² Progress is measured by the following milestones: (1) IAIS self assessment, (2) Strategy draft/proposal, (3) road map to IAIS compliance (4) statistical reporting system identified.

³ Progress is measured by the following steps (1) Investment Guidelines improved; (2) Investment Policy Statement developed; (3) Investment Committee established; (4) Investment Reports Improved; (5) Portfolio Management Procedures improved; (6) Insured Deposit Claims Payout Procedures improved; (7) Implementation Follow up

A new financial model for the calculation of deposit insurance premiums, forecasting cash flow and analyzing risk was developed and presented to the DIA/CBBH representatives during the workshop conducted on April 27, 2010 in Mostar. The model was finalized and used by the DIA to determine deposit insurance premium for 2011.

Indicator 15 : Number of pilot internal audit departments established in government and/or public enterprises

Results Summary

Y3 Result	1	Y3 Target	1	LOP Target	1
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Internal audit department in public utility company Rad was fully established

Indicator 17 (F Indicator 4): Number of national legislators and national legislative staff attending USG sponsored training or educational event

Results Summary

Y3 Result	8	Y3 Target	12	LOP Target	80
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In total, eight national legislative staff members attended the following workshops/sessions organized by the PARE project:

Workshop

-Risk Management -September 3, 2010.

Sessions

-FCU session with Peter Nicholl -October 22, 2010

-FCU session with Velimir Sonje -November 26, 2010

Participants included three men and five women from the Ministry of Finance and Treasury of BiH.

Indicator 18 (F Indicator 2): Number of financial-sector professionals trained on international standards this year with USG assistance

Results Summary

Y3 Result	96	Y3 Target	109	LOP Target	328
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In total 96 professionals attended the following workshops organized by the PARE project:

Workshops

- Basel II Market Risk (CBBH) -April 22, 2010

- Banking Reform Committee Session (UBBH) -July 22, 2010

- Risk Management – September 3, 2010

Training

- Risk Assessment, Rad company - September 27-29, December 1, 2010, December 6-8, 2010 and December 14-16, 2010

Technical meetings

- Basel II Standards implementation in BH banks- November 2010-March 2011

- Presentation of FDC concept –February 16, 2011

The participants list included 50 men and 46 women from the following institutions:

- 9 from CBBH
- 4 from associations (UBBH, Insurance and Leasing Association)
- 27 from commercial banks
- 56 from Rad company

Indicator 20: Glossary of Financial Terms developed (yes/no)

Results Summary

Y3 Result	0.4	Y3 Target	1	LOP Target	1
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97 items/financial terms (of planned 200) were collected in English language

Indicator 21: Progress⁴ toward private sector engagement in banking supervision reforms through UBBH

Results Summary

Y3 Result	2	Y3 Target	2	LOP Target	3
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UBBH established the Banking Reforms Committee (BRC) on its constitutional meeting held on May 26, 2010. The BRC work/action plan for banking reforms was developed and confirmed on July 22, 2010.

Indicator 22: Progress⁵ toward establishment of banking Supervision Council (BSC)/Financial Development Council (FDC)

Results Summary

Y3 Result	2	Y3 Target	2	LOP Target	3
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A concept paper on BSC/FDC was updated and revised in February 2011. The scope of BSC was expanded to non-banking components of the financial sector. A working group was established in March 2011.

Indicator 23: Progress⁶ toward building capacity of the BiH Ministry for Finance and Treasury

Results Summary

Y3 Result	2	Y3 Target	2	LOP Target	3
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Capacity needs have been identified, financial coordination unit structure proposed, and action plan prepared (as an integral part of MFT Capacity Building Inception report) in January 2011.

⁴ Progress is measured by the following milestones: (1) action plan developed, (2) UBBiH committee for banking supervision reform established, (3) implementation stage.

⁵ Progress is measured by the following milestones: (1) concept paper on BSC/FDC updated, (2) working group within Ministry of Finance and Treasury fully established, (3) draft law on BSC/FDC updated, (4) bill of law on BSC/FDC prepared.

⁶ Progress is measured by the following milestones: (1) capacity needs identified, (2) action plan prepared, (3) financial unit organization structure proposed (4) implementation stage.

ANNEX 2 – LIST OF COUNTERPARTS

PIR 1: Regulatory System for Financial Services Sector Strengthened

KRA 1.1: Banking supervision improved

Institution	Town	Address	Tel/Fax	Web site
Banking Agency of the Federation of Bosnia and Herzegovina Agencija za bankarstvo Federacije Bosne i Hercegovine (FBA)	Sarajevo	Koševo 3	033 721 400	www.fba.ba
Banking Agency of the Republic of Srpska Agencija za bankarstvo Republike Srpske (ABRS)	Banja Luka	Vase Pelagića 11 A	051 218 111 051 216 665	www.abrs.ba

KRA 1.2: Insurance supervision improved

Institution	Town	Address	Tel/Fax	Web site
Insurance Agency of Bosnia and Herzegovina Agencija za osiguranje u Bosni i Hercegovini	Sarajevo	Obala Kulina Bana 4/II	033 554 795 033 554 796	www.azobih.gov.ba
Insurance Supervisory Agency of the Federation of Bosnia and Herzegovina Agencija za nadzor osiguranja Federacije Bosne i Hercegovine	Sarajevo	Dolina 8/II	033 443 292 033 443 318	www.nados.ba
Insurance Agency of the Republic of Srpska Agencija za osiguranje Republike Srpske	Banja Luka	Bana Milosavljevića 8/II	051 228 910 051 228 920	www.azors.org
Protection Fund of the Federation of Bosnia and Herzegovina Zaštitni Fond Federacije Bosne i Hercegovine	Sarajevo	Mis Irbina 5	033 213 723	
Protection Fund of the Republic of Srpska Zaštitni Fond Republike Srpske	Banja Luka	Solunska 10	051 226 091	

KRA 1.3 - Capital market's surveillance capacity and compliance with standards improved

Institution	Town	Address	Tel/Fax	Web site
Securities Commission of the Federation of Bosnia and Herzegovina Komisija za vrijednosne papire Federacije Bosne i Hercegovine	Sarajevo	Čemaluša 9/II	033 203 862 033 211 655	www.komvp.gov.ba
Securities Commission of the Republic of Srpska Komisija za hartije od vrijednosti Republike Srpske	Banja Luka	Vuka Karadžića 6	051 218 362 051 218 361	www.sec.rs.ba
The Sarajevo Stock Exchange – SASE Sarajevska berza/burza vrijednosnih papira	Sarajevo	Đoke Mazalića 4	033 251 460 033 559 460	www.sase.ba
Banja Luka Stock Exchange – BLSE Banjalička berza hartija od vrijednosti	Banja Luka	Petra Kočića bb	051 326 041 051 326 056	www.blberza.com

KRA 1.5: Deposit Insurance Agency's investment strategy, deposit threshold model, and deposit premiums updated

Institution	Town	Address	Tel/Fax	Web site
Deposit Insurance Agency of Bosnia and Herzegovina (DIA) Agencija za osiguranje depozita Bosne i Hercegovine	Sarajevo	Jadranska bb	033 663 095 033 220 308	www.aod.ba
	Banja Luka	Vase Pelagića 11a	051 223 440 051 223 452	

KRA 1.6 Private Pension Fund Development Fostered

Institution	Town	Address	Tel/Fax	Web site
Securities Commission of the Federation of Bosnia and Herzegovina Komisija za vrijednosne papire Federacije Bosne i Hercegovine	Details are stated in KRA 1.3			
Insurance Agency of the Republic of Srpska Agencija za osiguranje Republike Srpske	Details are stated in KRA 1.2			
Pension Reform Commission of the Federation of Bosnia and Herzegovina Komisija za reformu penzionog sistema Vlade Federacije BiH	Sarajevo	Ložionička 2	033 723 131 033 723 200	

KRA 1.7: Central Bank alignment with EU best practices improved

Institution	Town	Address	Tel/Fax	Web site
Central Bank of Bosnia and Herzegovina (CBBH) Centralna Banka Bosne i Hercegovine	Sarajevo	Maršala Tita 25	033 278 201 033 201 517	www.cbbh.ba

Institution	Town	Address	Tel/Fax	Web site
Ministry of Finance and Treasury of Bosnia and Herzegovina Ministarstvo finansija i trezora Bosne i Hercegovine	Sarajevo	Trg BiH 1	033 205 345 033 202 930	www.trezorbih.gov.ba
Ministry of Finance of the Federation of Bosnia and Herzegovina Ministarstvo finansija Federacije BiH	Sarajevo	Mehmeda Spahe 5	033 253 532 033 253 400	www.fmf.gov.ba
Ministry of Finance of Republic of Srpska Ministarstvo finansija Republike Srpske	Banja Luka	Vuka Karadžića 4	051 331 350 051 331 351	www.mf.vladars.net

PIR 2: Financial Administration of Public Resources Improved

KRA 2.1 Parliamentary committees overseeing public-sector audits enhanced

Institution	Town	Address	Tel/Fax	Web site
Committee for Finance and Budget House of Representatives of BiH Parliamentary Assembly Komisija za finansije i budžet Predstavničkog doma Parlamenta BiH	Sarajevo	Trg BiH 1	033 284 437 033 233 480	www.parlament.ba
Committee for Finance and Budget House of Peoples of BiH Parliamentary Assembly Komisija za finansije i budžet Doma naroda Parlamenta BiH	Sarajevo	Trg BiH 1	033 284 463 033 233 480	www.parlament.ba
Joint Audit Committee - Parliament of the Federation of Bosnia and Herzegovina Zajednička Komisija za reviziju Parlamenta Federacije Bosne i Hercegovine	Sarajevo	Hamdije Kreševljakovića 3	033 203 658	www.parlamentfbih.ba
Audit Committee of the National Assembly of Republika Srpska Odbor za reviziju Narodne Skupštine Republike Srpske	Banja Luka	Vuka Karadžića 2	051 338 115	www.narodnaskupstinars.net

KRA 2.2 Public awareness of audit findings improved

Institution	Town	Address	Tel/Fax	Web site
Audit Office of the Institutions of Bosnia and Herzegovina Ured za reviziju institucija Bosne i Hercegovine	Sarajevo	Hamdije Čemerlića 2/XIII	033 703 573 033 703 565	
Audit Office for the Institutions of the Federation of Bosnia and Herzegovina Ured za reviziju institucija u Fedearciji Bosne i Hercegovine	Sarajevo	Ložionička 3	033 723 550 033 716 400	www.saifbih.ba
The Supreme Office for the Republic of Srpska Public Sector Auditing Glavna služba za reviziju javnog sektora Republike Srpske	Banja Luka	Vuka Karadžića 4	051 247 408 051 247 497	www.gsr-rs.org

KRA 2.3 Pilot internal controls and audit units established

Institution	Town	Address	Tel/Fax	Web site
City of Banja Luka Grad Banja Luka	Banja Luka	Trg srpskih vladara 1	051 244 444 051 244 546	www.banjaluka.rs.ba
IIA Institute of internal auditors of Bosnia and Herzegovina Institut internih revizora Bosna i Hercegovina	Sarajevo	Dolina 2/II, Marijin Dvor	033 251 700 033 251 701	www.interni-revizori.info

PIR 3: Enabling Environment for Private Sector Investment Improved

KRA 3.2: Capacity of financial services professional associations enhanced

Institution	Town	Address	Tel/Fax	Web site
Association of Accountants, Auditors and Financial Professionals of the Federation of Bosnia and Herzegovina Savez računovođa, revizora i finansijskih djelatnika u Federaciji Bosne i Hercegovine	Mostar	Kneza Višesalava 77 a	036 318 660 036 334 184	www.srr-fbih.org
Association of Accountants and Auditors of the Republic of Srpska Savez računovođa i revizora Republike Srpske	Banja Luka	1 Krajiškog korpusa 16/III	051 430 190 051 430 200	www.srrrs.org
Association of Court Experts of the Republic of Srpska Udruženje sudskih vještaka Republike Srpske	Banja Luka	Vladike Platona 3	051 218 005 051 218 005	
Association of Court Experts of the Federation of Bosnia and Herzegovina Udruženje sudskih vještaka Federacije Bosne i Hercegovine	Sarajevo	Ložionička 12	061 147 744 033 650 301	www.udruzenje-vjestaka.com
Association of Leasing Companies of Bosnia and Herzegovina Udruženje društava za leasing u Bosni i Hercegovini	Sarajevo	Zmaja od Bosne 4	033 202 741 033 202 741	
Banks Association of Bosnia and Herzegovina Udruženje/Udruga banaka Bosne i Hercegovine	Sarajevo	Fra Anđela Zvizdovića 1/X	033 296 502 033 296 509	www.ubbih.ba
Association of Microfinance Institutions in Bosnia and Herzegovina Udruženje društava mikrofinansijskih institucija u Bosni i Hercegovini	Sarajevo	Branilaca Sarajeva 20	033 205 133	www.amfi.ba

ANNEX 3 – SUCCESS STORIES



USAID
FROM THE AMERICAN PEOPLE

BOSNIA-HERZEGOVINA

SUCCESS STORY

Interactive Technologies for Banking Supervision



Facilitated Creation of Basel II Web Portal

The Basel II web page
is accessible at:
www.bankarska-supervizija.info

USAID PARE launched a specially designed web portal to facilitate the exchange of information between the BiH financial institutions (FI) on policy and regulatory issues related to the implementation of the Risk Based Supervision in BiH (Basel II Framework).

The purpose of the web portal is to store and facilitate the exchange of key documents and relevant information between the FIs' working groups and key stakeholders in financial sector services. It contributes to a more efficient process of the Basel II Framework implementation in terms of knowledge transfer and management, presentation and internal consistency of relevant information.

The portal contains information and records about the conclusions and observations stemming from the ongoing work of the working groups, results of joint assessments and decisions on the supervisory procedures, as well as up-to-date references about the latest regulatory developments in the EU and internationally.

The portal's design was inspired by the Committee of European Banking Supervisors' (CEBS) website. Its structure is similar to the one used by the EU member countries to publish their regulatory information, which enables the BiH banking supervisors to publish the new regulatory framework information in a standardized format

Basel II Framework for Bosnia and Herzegovina

Okvir Basela II / Basel II Framework

- Strategija / Strategy
- Akcionni Plan / Action Plan
- Struktura i članovi radnih grupa / Working groups structure and membership
- Nova kategorija / New categorie

Aktivnosti Radnih Grupa / Working Groups Activities

- Stup I / Pilar I
- Trzinski Rizik / Market Risk
- Operativni Rizik / Ops Risk
- Kreditni Rizik / Credit Risk
- Kapital / Own Funds
- Stup II / Pilar II
- Stup III / Pilar III
- Radne Grupe / Working Groups
- Nova kategorija / New categorie

Supervizorske objave / Supervisory disclosure

- Supervizorski pregled / Supervisory review
- Regulatorni Impact / Regulatory Impact
- Opcije i diskrecije država / Options and national discretions
- Nova kategorija / New categorie

CEBS Linkovi / CEBS Links

- Supervisory Colleges
- Cross sector cooperation
- Nova kategorija / New categorie

Plan obuke / Training Plan

- PARE Training

Okvir Basela II / Basel II Framework - Akcionni Plan / Action Plan

AKTIVAN / ACTIVE

Novi dokument / New document

Action Plan / Action Plan - Ver 4, 03Feb2010
download newbaselIIOkvirBIH_akcionPlan_ver4_2010feb03.doc - 12/04/2010 03:53

Strategija Agencije za bankarstvo FBiH
download Strategija FBA bhs - 12/04/2010 03:52

Strategija Agencije za bankarstvo FBiH
download Strategija FBA en - 12/04/2010 03:52

Strategija Agencije za bankarstvo RS
download Strategija ABRS - 12/04/2010 03:50

ARHIVA / ARCHIVE

Novi dokument / New document

Action Plan / Action Plan - Ver 3, 28Oct2010
download akcionPlan_ver3.doc - 28/10/2009 03:58

REFERenca / REFERENCE

Novi dokument / New document

Okvir Basela II za BiH / Basel II Framework for BiH - Presentation
download pare_b2f_presentation - 13/04/2010 16:57

U.S. Agency for International Development
www.usaid.gov



USAID
FROM THE AMERICAN PEOPLE

BOSNIA-HERZEGOVINA

SUCCESS STORY

Improving Internal Audit Functions

Developing of Set of Documents Improves Internal Audit Operations in Public Sector



*Rad Strategic Audit Planning Workshop
2010*

“As a certified auditor, I found this assistance important for a better and more efficient operations of the “RAD”, stated the Head of Accounting Department with “RAD”.

U.S. Agency for International Development
www.usaid.gov

The overall objective of USAID PARE’s assistance in Component 2 is to improve the financial administration of public resources, including establishment of internal audit (IA) units in the public enterprises and/or government offices. In September 2010, PARE selected a public utility enterprise, “RAD”, to set up a pilot IA unit in support of the development and strengthening of IA functions. Designed to measure the efficiency of operations, the reliability of financial reporting, deterring and investigating fraud, safeguarding assets, and compliance with laws and regulations, the IA unit is meant to help organizations achieve stated objectives. It does this by using a systematic methodology for analyzing business processes, procedures, and activities, with the goal of highlighting organizational problems and recommending solutions.

In that regard, USAID PARE has provided technical assistance that will enable the selected IA unit to introduce international and advanced practices in its internal audit operations. In addition, USAID PARE worked with the selected IA unit to develop a set of documents, including a risk assessment framework, risk-based strategic and annual audit plan, audit report with recommendations, quarterly and annual report, and standardized legal and other documents required by law and other applicable provisions. These documents are important tools for the IA unit to increase its capacity and improve its internal audit functions. One specific activity included the education and presentations for the IA unit and senior staff with “RAD” on international best practices in internal audit functions and the role of the internal audit.

Commenting on USAID PARE’s technical assistance to the IA unit, and in particular the educational component of the assistance, Jasmina Gacanovic, Head of the Accounting Department at “RAD”, stated, “As a certified auditor, I found this assistance important for a better and more efficient operation of the “RAD”. Some of the attained experiences involved in strategic planning will help me to achieve the goals defined in the action plan. I find that the similar opportunities in the future will be very useful”.

This IA pilot unit is meant to serve as a model unit and IA documents can easily be replicated in all other similar public companies, institutions, and agencies in BiH. As continuation, PARE intends to organize a follow up round table to present experiences and disseminate the developed IA documents and templates.

ANNEX 4 – US STUDY TOUR REPORT - EXCERPT

Introduction

USAID PARE facilitated a study tour of Bosnia-Herzegovina (BiH) financial regulators to the United States that took place from February 5 - 17, 2011.

The group visited US Federal and State regulators and supervisors in Washington, DC, and New York City – the Federal Reserve, the Federal Reserve Bank of New York, the US Treasury, the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Commission (FDIC), the Federal Financial Institutions Examination Council (FFIEC), the National Association of Insurance Commissioners (NAIC), the New York State Banking Department, representatives of international financial institutions, the World Bank and the International Monetary Fund (IMF), representatives of USAID, as well as representatives of financial market professional associations, such as, the Securities Industry and Financial Market Association (SIFMA), Financial Industry Regulatory Authority (FINRA), and US-based think tanks and members of the academic community.

The study tour's main objective was to familiarize BiH financial regulators from the banking and insurance industries with financial policies and governance in the United States, including ongoing regulatory changes in the wake of the recent financial crisis. The BiH regulators had a unique chance to learn about the US regulatory framework, new developments following the passage of the Dodd-Frank Act into law, and the challenges faced by US regulators as they continue to mitigate the effects of the financial crisis and work to prevent a future recurrence.

The ten-day tour offered the group a chance to learn about developments across the entire US regulatory spectrum, on the Federal and State level, from non-government perspectives, and from banking and key non-banking regulators. The wide variety of institutions and meetings over the ten-day period allowed the group to grasp the complexity and significance of new US regulatory reforms and to gain enough understanding of the Dodd-Frank Act to be able to discuss implementation issues with the institutions with which they met.

The high concentration of meetings in a short period of time was a rare opportunity to gain a comprehensive understanding of the processes and institutions involved in formulation and implementation of macroeconomic policy and financial-regulatory reform in the United States. The tour's lessons learned regarding US regulation provide insight for comparing and contrasting to key aspects of international standards in financial sector regulation and supervision. This provided the group with questions and ideas for extensive internal discussions and deliberation regarding how BiH institutions fare in comparison to their US counterparts, and how US experiences can be modified for application in BiH.

Summary of Meetings

The meetings yielded various perspectives on the structure, composition, status, and development of the US regulatory framework. Specific regulatory developments discussed included the implementation of the Dodd-Frank Act, the US position regarding Basel II/III developments, and the effects these developments may have on global markets. The

meetings enabled the group to establish useful contacts and supervisory links that will promote future cooperation, technical assistance, and supervisory coordination. The meeting with USAID Washington offered an exclusive opportunity for the participants to communicate their experience and satisfaction with the technical assistance extended through USAID PARE

Monday, February 7, 2011

World Bank

The delegates had their first meeting at the World Bank with Mr. Lalit Raina and Ms. Aurora Ferrari. The group discussed the World Bank's ongoing programs and the possibility of extending technical assistance (TA) to other areas of the BiH financial system. For example, technical assistance to introduce International Financial Reporting Standards (IRFS) was mentioned as an opportunity for World Bank engagement in BiH. The assistance could be extended through the Bank's Vienna-based team. Mr. Raina and Ms. Ferrari stipulated that as a precondition to receiving World Bank TA, the BiH authorities would need to submit to the Bank a formal letter requesting specific assistance.

USAID

The delegates received a formal welcome from several members of USAID Washington, including the Director of the Economic Growth Office involved in finance development projects world-wide. The meeting reviewed the extent and achievements of USAID TA to the BiH financial sector from 1996 to the present day. The delegates, in particular, praised the assistance of the USAID PARE project, listed several successes and accomplishments in regulatory reforms, answered many questions from USAID Directors, and expressed interest in the extension of TA to continue covering financial sector reforms. USAID E&E/EG Economic Growth Officer Ms. Sara Keefe joined the participants for a part of the program with other institutions and was pleased by the informative nature of the meetings.

International Monetary Fund

The delegates met with several representatives of the International Monetary Fund (IMF) Monetary and Capital Department Financial Oversight Division, including Senior Financial Experts David Parker and Jennifer Elliot. The participants were presented with the IMF's efforts to address the financial crises, proposals to strengthen financial regulations, and financial system oversight to preserve stability. The presentations covered a wide range of topics from Basel II/III developments, Financial Stability Board (FSB) activities, the IMF's role in these it, and the new global regulatory structures that will allow more oversight and compliance by IMF member countries. The delegates discussed BiH activities to combat the crisis and described their experience with Basel II/III standards from the point-of-view of smaller, open economies. A comprehensive presentation was also provided of the deposit insurance principles, practices and plans for their introduction. The BiH DIA Director shared that the Deposit Insurance scheme in BiH, strengthened through USAID PARE TA, already observes the core principles, which received praise from the IMF representatives.

The Federal Reserve Board

At the meeting with the Federal Reserve Board, delegates viewed a presentation on the US Federal Reserve System functions and responsibilities, including how the Board functions as part of the US financial system, setting monetary policy, and providing supervision and regulation, including the structure of the US financial regulatory framework and the Board's existing and new roles since the onset of the financial crisis. The Board's representatives discussed the important regulatory reforms under the Dodd-Frank Act and the effect these changes may have on developing economies. The Board described the new position of Systemically Important Non-bank Financial Institutions (SIFIs), the expected effects of the new leverage regime, and the effects the new regulatory regime of the SIFIs may have on the US and the global markets. The complexity of the Dodd-Frank Act implementation was highlighted with the fact that there are 260 separate complex projects that need to be implemented by a wide range of the US regulatory institutions by July 2011. Finally, the Board presentation described how supervision will be extended to the shadow banking and non-banking sectors, citing as an example the establishment of a new insurance supervision office at the Board, as a new Federal level body. Participants also learned about the Federal Reserve System examiner training programs and received a course catalogue of the supervisory and regulatory trainings which will be offered in 2011.

National Association of Insurance Commissioners (NAIC)

The delegates met with five representatives of the NAIC, Associate Commissioner for Insurance Philip Barlow, Government Relations Director Ethan Sonnichsen, Government Relations Manager Moira Campion, International Relations Counsel and Manager George Brady, and International Policy Analyst Ekrem Sarper. The representatives provided a presentation and led discussion of the structure of insurance supervision in the US, the Association's role in the American financial system, the types of support the NAIC provides to insurance regulators and changes which have taken place in insurance regulation since the financial crisis. The NAIC provided an overview of how insurance supervision functions with Federal regulation is being transposed to the State level and implemented in more than 50 US jurisdictions. The NAIC highlighted the fact that the US insurance market is the most developed in the world, with over six trillion dollars in assets and 1.7 trillion dollars in annual gross premiums. They stressed the complexity of the insurance sector and the greater oversight to which it has always been subject, in contrast to the banking industry and banking supervision which is only now being ramped up in light of the financial crisis. They stated that insurance companies have maintained good financial standing throughout the crisis. Furthermore, the NAIC presented information about types of insurance that are not in use in BiH, for example, title insurance. BiH Insurance Agency Director Samir Omerhodzic described the structure of insurance supervision in BiH, within the broader context of the BiH financial system and described the level of development of the BiH insurance market. The NAIC expressed willingness to provide direct TA to BiH supervisors and maintain supervisory contact, despite no US companies operating in the BiH insurance market.

Office of the Comptroller of the Currency (OCC)

The delegates met with OCC representatives Maria G. Arevalo, Susan Quill, and Rick Gaffin, to discuss the OCC's role in the supervision of the national banking system, their work in relation to that of the other supervisory bodies, supervision of branches of foreign banks, and coordination with international committees such as the Basel Committee. The delegates received a compact disc with a compilation of all relevant regulatory documents. In regards to Dodd-Frank implementation, the representatives remarked that the OCC supervises the largest banks in the system, institutions that are the core focus of the Dodd-Frank regulatory changes. They pointed out that about 25 percent of all projects to implement Dodd-Frank are the direct responsibility of the institution. Following the ongoing restructuring of the US regulatory framework, it is expected that the Office of Thrift Supervision (OTS) will become a part of the OCC.

Wednesday, February 9, 2011

Financial Industry Regulatory Authority (FINRA)

The delegates met with FINRA representatives, Ms. Jeanne Balcom, Mr. Steven Polansky, and Mr. Michael Kulczak to discuss the Agency's role in US capital market oversight. FINRA made a detailed presentation of the US regulatory structure, the institutions involved, FINRA's role and structure, and the rules governing Self Regulatory Organizations (SROs). FINRA exercises surveillance over 500,000 persons, registered market participants and over 4,000 firms and is in turn overseen by the Securities and Exchange Commission (SEC). Using the Trade Reporting and Compliance Engine (TRACE) which is accessible through the FINRA website, FINRA members are required to report the price of over-the-counter corporate bonds, to maintain transparency. On the regulatory side, FINRA is an active member of the International Organization of Securities Commission (IOSCO) and is participating in developing standards and principles, and works to create transparency in and regulate "dark pool" segments of markets. FINRA also levies fines and other penalties on market participants, and works with the Federal and State prosecutors offices, police forces and courts to process financial crimes cases in courts. It has also provided technical and capacity building assistance to international law enforcement agencies and judges (Croatia, Slovenia, etc.) to improve their ability to process financial crimes. Finally, FINRA has integrated consumer protection offices and acts as an ombudsman and transparency advocate in this area to prevent fraud, bad practices and protect interests of small investors, represented largely by retail transactions.

The United States Treasury

The meeting with the US Treasury representatives covered the background and origins of the financial crisis, the Treasury's role in preserving financial stability and its efforts to restructure financial oversight. Paul Leonovich, Associate Director for Banking & Financial Services in the Office of Technical Assistance described the events and development since the onset of the crisis. Christopher Smart, Deputy Assistant Secretary for Europe and Eurasia, talked about the new regulatory reforms and the US role in the international developments. He discussed the setup and operations of the Financial Stability Oversight Council (FSOC), a new oversight body chaired by the US Treasury Secretary. Susan Baker, director of the Office of International Banking and Securities Markets, described the US role in Basel III developments and international cooperation between supervisors from G20 countries to provide guidance in the new risk-prudential

global regulatory environment. The group also received a fascinating historical tour of the US Treasury building. Prior to the Treasury visit, the participants enjoyed and greatly benefited from lunch and informal discussions with Paul Leonovich, Laura Trimble, Associate Director of the US Treasury Office of Technical Assistance, and Thomas Briggs, USAID Washington Senior Policy Advisor.

Thursday, February 10, 2011

Federal Financial Institutions Examination Council (FFIEC)

The delegates learned about the structure and organizational set-up of the FFIEC and the Council's practice of providing examination guidance for agencies' financial regulation, and information on consumer compliance. The FFIEC is comprised of members of relevant financial regulatory institutions and brings all supervisory information in one place offering the regulators a comprehensive look at banks' standing in the financial sector. Work is done through six task forces covering a range of regulatory and oversight issues, while the scope remains limited to deposit-taking institutions. The new FSOC covers a wider range of the financial sector than the FFIEC, because it includes insurance supervision and regulators.

The FFIEC's Uniform Bank Performance Report (UBPR) report collects banks' quarterly call report data, and processes it automatically to generate analytical and decision-making reports and results. It offers a series of summary reports to regulators enabling them to make decisions regarding the examination of individual banks and oversight actions, and to observe the overall health of the banking sector. The FFIEC also works on consumer protection issues providing wider scope and coverage of these issues. Finally, the FFIEC in combination with the FDIC has a separate educational component offering a wide range of courses in different areas of finance for the regulators in US and internationally. The delegates learned that they would be eligible for some of these course offerings.

Meeting with the Federal Deposit Insurance Corporation (FDIC)

The delegates meet representatives of the FDIC including a bank examiner, international affairs representatives, and legal advisers. The FDIC first presented an overview of the bank examination process and ongoing supervision of financial institutions. The delegates discussed the key aspects of the onsite and offsite inspections, drew comparative conclusions and discussed regulatory aspects of FDIC and BiH agencies examination work. In contrast to the situation in BiH where the Deposit Insurance Agency DIA does not have authority to supervise the banking system a great deal of the FDIC responsibilities includes oversight over the large number of banks.

The FDIC's legal representatives presented details of Dodd-Frank implementation, drawing conclusions on the eventual impact its implementation could have on economies internationally. As the FDIC is one of the key financial institutions in the US, its representatives described the specific burdens of Dodd-Frank implementation in terms of the increased work-load, drafting new regulation, and implementing projects, which should be completed by July 2011. The delegates inquired about the treatment of different

classes of bank stakeholders, such as depositors, covered creditors, equity holders, etc, and compared the legal set-up and practices of the two countries.

Friday, February 11, 2011

Securities Industry and Financial Markets Association (SIFMA)

The delegates met with the Managing Director of SIFMA for a detailed discussion of the U.S. financial market, reform efforts, and Basel regulations. SIFMA presented its structure, mission and activities, including its goals during Dodd-Frank drafting and discussions. SIFMA is working to enable market participants, its members, prepare to implement a myriad of new regulations and regulatory requirements. The discussion centered on the considerations in categorizing Systemically Important Financial Institutions (SIFIs) which are then subject to a new set of regulations, including higher capital and liquidity requirements, restrictions on future mergers, acquisitions, living wills requirements, and forced dissolution. The discussion then turned to the ongoing development of Basel III requirements, the association's role in that process, and the industry's opinion of the upcoming regulatory changes. The discussion offered a unique industry point-of-view, the challenges and limitations posed by regulators, and the new nature of international relations and their effect on the US marketplace.

Monday, February 14, 2011

Federal Reserve Bank of New York

The delegates met with Howard Howe, the assistant vice-president of the International Affairs Function of the Federal Reserve Bank of New York, a permanent voting member of the Federal Reserve's Board of Governors and a key institution in creating and implementing US monetary policy. The group learned in detail how the Federal Reserve makes regulatory decisions, the structure of the US-wide decentralized system of Federal Reserve Banks and reinforced information from previous meetings regarding various aspects of regulatory reforms in the US. Mr. Howe presented the ways the Federal Reserve managed the US economic and financial environment throughout the crisis. The presentation included a detailed overview of regulatory, macro-prudential and monetary responses. He also offered an effective visual representation of the Federal Reserve's expanding balance sheet, and monetary strategy for combating the global financial crisis, and context regarding the first and second large-scale asset purchases (QE - quantitative easing) and the strategy for US economic recovery.

Roosevelt Institute / Institute of New Economic Thinking

At the Roosevelt Institute the delegates met with Executive Director Mr. Robert Johnson and Institute Fellow Mr. Michael Konczal. Mr. Johnson began the discussion by outlining the shortcomings which the Roosevelt Institute sees in the latest financial reform and sharing information about some of the Institute's recent publications. In comparison to the measured optimism which many regulatory institutions expressed regarding reform and the outlook for the US economy, the Institute felt that the country still lacked appropriate

economic solutions. His focus and that of Mr. Konczal was on the effects of the financial crisis in the consumer economy and in daily lives of Americans rather than on the institutional level.

Tuesday, February 15, 2011

New York University

The delegates met with Dr. Paul Wachtel, a former World Bank and IMF consultant and advisor to the Central Bank of Croatia, now a professor of development economics at the Stern School of Business at New York University. In light of the global financial crisis and economic shifts due to globalization, Dr. Wachtel stated that development economics is no longer a field which is only applicable to certain countries, but now relevant worldwide and bears implications for “developed” countries. In this context the group discussed ideas they had heard over the course of the tour in regards to U.S. regulatory developments. He also discussed his experience working in Croatia and lessons learned which are applicable to the Bosnian context, particularly central banking and monetary policy in the CEE region.

State of New York, Superintendent of Banks

The delegates met with the Richard H. Neiman, Superintendent of Banks and multiple members of the senior staff. The meeting began with a presentation of the institution's structure and approach to supervision of the most important financial market in the US and worldwide. Having decision-makers present from both a Bosnian and a U.S. State supervisory institution, and because the BiH delegates being well-versed in U.S. regulation after their week of meetings, allowed for an extremely productive exchange of ideas. The Superintendent welcomed the opportunity to discuss recent state-level developments and their experiences from the past several years and was very interested to hear about the experiences of a small, open economy and the performance of European banks in the BiH markets. Finally, even though none of the US banks operates in the BiH market, and vice-versa, the New York State Bank supervisors offered to establish and formalize supervisory cooperation with their Bosnia colleagues.

Participant Feedback

Josip Nevjestic, Director of the Deposit Insurance Agency of BiH

The IMF's presentation of the new International Principles for Deposit Insurance was very informative and showed us that we have largely implemented all international best practices and complies with the principles, despite being a relatively new deposit insurance agency and scheme.

Samir Omerhodzic, Director of the Insurance Agency of BiH

The visit [with the NAIC] has confirmed that the insurance sector was not as affected by the crisis as the banks were – what's more growth was recorded in the US insurance sector in the past period.

Slavica Injac, Director of Banking Agency of Republika Srpska

I have to say that it was a big privilege for us to meet representatives of the key financial institutions in the States who unselfishly and openly spoke not only about their experiences, their knowledge but also their challenges.

Zlatko Bars, Director of Banking Agency of FBiH

The visit to the U.S. Treasury has confirmed, despite popular belief that the US is working to implement advanced approaches for internationally active banks, in accordance with the strategy of Basel Core Principles implementation set by the BIS.

Anka Musa, Advisor to the CBBH Governor

The visit to the Federal Reserve Board and the Reserve Bank of New York gave us a perfect view on the methods of management and decision-making at the Federal Reserves and of the general monetary policy in the US.

ANNEX 5 – TRAINING ACTIVITY SUMMARIES

Market Risk Team Formation

April 20, 2010
Jahorina, BiH

As a part of USAID ongoing technical assistance to BiH financial sector regulators, PARE facilitated the foundation of the Market Risk Team comprised of representatives from the Central Bank of BiH and the entity-level Banking Supervision Agencies in BiH. The group is the first risk-based supervisory team formed and is charged with leading the development and supervision of all market and liquidity risk oversight methodologies on a bank-by-bank basis. Under the auspices of PARE, the team forms the foundation of the program to develop best practices in risk management in banks and augment supervisory methods and expertise in these topics. During their first working session on April 20, 2010, the market risk team set up tasks for the next two quarters.



PARE facilitated Market Risk Team Formation, April, 2010

Ema Fiser Proho, a newly appointed Team Coordinator, said: "I find today's event an excellent opportunity to further extend my knowledge and gain more practical experiences in market risk and liquidity oversight"

Financial Model for Calculation of Deposit Insurance Premiums

April 27, 2010
Mostar, BiH

As a continuation of the technical assistance in the deposit insurance sector, PARE organized a workshop on financial modeling for calculation of deposit insurance premiums for staff of the deposit Insurance Agency of BiH (DIA). The goal of the workshop was to train the DIA staff on how to use the new model and ensure the feasibility of DIA's continuous administration of the model. The participants will continue to work with PARE on implementation of the integrated financial planning model.



DIA representatives attend the workshop on financial modeling for calculation of deposit insurance premiums, April, 2010

DIA Director Josip Nevjestic said that "Today's presentation proved to be a great opportunity for us to learn more about this model that will help us to calculate insurance deposit premiums and define insurance limits in order to present them to the DIA's Managing Board meeting in October 2010."

Market Risk Work Team - Session II

July 7-8, 2010

Teslić, BiH

On July 7-8, 2010, PARE concluded a successful second working session of the Market Risk Team (MRT) in Teslić. Following the conclusions of the April meeting, when the MRT was formed, the team continued to work on the specific tasks related to development and supervision of market risk processes on a bank-by-bank basis. The second session discussed the status of the team's efforts in completing the assigned tasks, evaluated the material gathered and identified next steps. The objectives of this session was to review the efforts of the team in collecting bank specific and systematic market risk data already available within the supervisory agencies and the central bank.



Market Risk Work Team - Session II, July, 2010

Eight participants attended the workshop, including representatives of the Central Bank BiH and entity-level banking agencies in BiH..

All attendees rated the workshop highly on evaluation forms

Banking Supervision Reforms - EU Directives and Risk Management

September 3, 2010

Sarajevo, BiH

The seminar was complimentary to technical assistance PARE provides to the banking supervisors, financial institutions, and private banking sector in BiH. This assistance is aimed to strengthen compliance with international standards for banking supervision. The goal of the seminar was to provide transfer of knowledge and experience to the regulators, supervisors, and other actors in the financial services sector of BiH on the latest changes in the banking regulation. A particular emphasis was put on risk management and changes in the EU banking regulatory framework. The seminar included participation of local and Slovenian banking and risk management experts.



Risk Management Workshop, Sarajevo, September, 2010

„Attendance of representatives of all relevant institutions in the financial sector in BiH including Banking Agencies in FBiH and RS, Ministry of Finance and Treasury of BiH, Central Bank of BiH, Deposit Insurance Agency of BiH, as well as commercial banks in BiH, proved the importance of today's seminar. The seminar was organized at the right time for those dealing with concrete issues related to the introduction of the EU directives in the banking supervision of BiH”, said one attendee.

The attendee emphasized that “the seminar provides an excellent opportunity for the regulators, supervisors, and other actors in the financial service sector in BiH to get a better understanding of the latest developments in the banking regulation in the EU”.

Letter of Intent on Cooperation between USAID PARE and the Ministry of Finance and Treasury of BiH

**September 7, 2010
Sarajevo, BiH**

On September 7, 2010, PARE and the Ministry of Finance and Treasury of BiH (MFT) signed a Letter of Intent (LoI), which opens opportunities for new collaborative activities to establish a formal and cooperative relationship between USAID PARE and the MFT to support capacity of the MFT to fully perform its regulatory and policy design role in BiH financial sector and to increase its ability for expertise and reporting on the developments in the financial sector of BiH.

This collaborative effort builds upon PARE's technical assistance to advance financial sector reform processes in support of a modern, stable and competitive financial sector in BiH. This assistance will create a more coherent financial sector in BiH, and will improve collaboration between the public financial institutions and the private sector. It also supports the Ministry's efforts to design forward looking financial policies aimed at sound financial sector development in BiH.



USAID Mission Director Allan Reed and Minister of Finance and Treasury of BiH Dragan Vrankic congratulate on the signing of letter of intent at a press event, September 7, 2010

*“The Letter of Intent on Cooperation between PARE and the Ministry of Finance advances financial sector reform processes in support of a modern, stable and competitive financial sector”,
said Mr. Reed*

Preparation of Internal Audit Risk Assessment and Internal Audit Strategic Plan On-the-job Training

**September 27-29, 2010
Sarajevo, BiH**

In September 2010 PARE selected a public utility enterprise “RAD” to set up a pilot internal audit (IA) unit to support development and strengthen IA functions.

In that regard, PARE provided an on-the-job training for the senior staff and members of the IA unit with “RAD” on international practices in internal audit operations. In addition, PARE worked with the selected IA unit to develop a set of documents including risk assessment framework, risk-based strategic and annual audit plan, audit report with recommendations, quarterly and annual report, and standardized legal and other documents required by law and other applicable provisions. These documents are important tools for the IA unit to increase its capacity and improve its internal audit functions.

This IA pilot unit is meant to serve as a model unit and IA set of documents/reports can easily be replicated in all other similar public companies, institutions and agencies in BiH in support of the development and strengthening of IA functions within the public institutions.



PARE and members of RAD pilot internal audit unit on Strategic Audit Planning On-the job training session, April 27, 2011



PARE and members speak about the international practices in internal audit operations

“As a certified auditor, I found this assistance important for more efficient operations of “RAD”. Some of the attained experiences involved in strategic planning will help me to achieve the goals defined in the action plan. I find that that the similar training opportunities in the future will also be very useful”, said the head of Accounting Department of “RAD”

DCA Loan Guarantee Program Signing Ceremony

**October 21, 2010
Sarajevo, BiH**

On October 21, 2010, his Excellency Ambassador of the United States to BiH, Patrick Moon, and, his Excellency Ambassador of Sweden to BiH, Bosse Hedberg, participated in a press event to mark the launch of the USAID-Sida loan portfolio guarantee agreements with Raiffeisen Bank dd Bosna i Hercegovina and Volksbank BH dd.

The joint USAID-Sida loan guarantee will help expand the ability of banks in Bosnia and Herzegovina to finance loans for small and medium-sized enterprises (SMEs).

The loan guarantee will unlock up to \$40 million of much-needed credit and will allow each of the banks to leverage \$20 million in financing for SMEs, thereby stimulating economic growth and jobs. This loan guarantee program in BiH is the first country program under the global memorandum of understanding that USAID and Sida signed in March of this year in Washington, D.C.



Deputy Director of Raiffeisen Bank BiH, Ambassador of the United States, Ambassador of Sweden, and Director of Volksbank BH address the media, October 21, 2010

"This loan guarantee program is unique: it is the first such program that the United States has done in direct collaboration with another donor, Sida, anywhere in the world. I congratulate everyone's hard work and creativity in making this happen. This example shows that, working together, Bosnia and the international community can come up with creative and strong solutions for advancing necessary reforms and catalyzing development", said his Excellency Ambassador of the United States".

Banking Supervision Coordination Meeting

**October 20, 2010
Sarajevo, BiH**

The PARE team with consultants and Lead Coordinators from the entity-level Banking Agencies in FBiH and RS, and the Central Bank of BiH met on October 20, 2010 in Sarajevo. The participants were informed of the recent regulatory updates in the area of EU banking supervision. They submitted the feedback from their institutions regarding the adopted Strategy for Implementation of the International Capital Accords. The adopted timeline and phases of implementation contained in the Strategy were reviewed and confirmed. It was concluded that both the Strategy and the Action Plan for its implementation were well designed to absorb the current and future regulatory advances in the EU and internationally.



The October 20, 2010 meeting of Lead Coordinators confirmed the timeline for implementation of the adopted Strategy for Implementation of the Revised International Capital Framework Accords (Basel II/III)

Banking Supervision Reforms – Market Risks Decree Study Tour

December 13-17, 2010

Ljubljana, Slovenia

The study tour provided an opportunity for the lead coordinators, banking supervisors and technical experts / specialists from the banking supervision agencies in Bosnia and Herzegovina to acquire a working knowledge of the concepts and processes involved in development of market risk decree, and issues involved in regulatory aspects of market risk. This study tour also aimed to build capacity and identify technical solutions for the banking supervision regulators to develop the regulatory documents (Market Risk Decree) including the recommendations resulting from the study tour.



Participants on Slovenia Study Tour, December 17, 2010

“This study tour provided us with the wonderful opportunity to learn more about the issues involved in implementation of relevant market risk and how they function in practice” , said one training attendee

US-based Study Tour for BiH Financial Regulators

February 5-16, 2011

Washington, DC and New York, NY

From February 5 - 16, 2011 PARE organized a study trip to Washington, D.C. and New York, NY, for BiH delegation of financial regulators including senior-level officials from the Banking Supervision Agencies of FBiH and RS (BSAs), the Central Bank of BiH (CBBH), the Deposit Insurance Agency of BiH (DIA), and the Insurance Agency of BiH, to observe the policies and governance that are key to the implementation of international standards in financial sector regulation and supervision and how these experiences can be applied in BiH.

In addition to providing general exposure to the US financial sector regulation and oversight, the program was built around visits to the federal institutions including, among others, the Federal Deposit Insurance Corporation (FDIC), Financial Industry Regulatory Authority (FINRA), Securities Industry and Financial Markets Association (SIFMA), the US Treasury, that are involved in formulation and implementation of macroeconomic and financial-regulatory reform and policies in the economic and financial sector. Particular attention of the study tour was paid to the future architecture of the global financial system and the new framework of regulation and supervision that can help maintain financial stability.

The training and exchange of information in developing and implementing international principles and standards in financial institutions regulation, as well as the identification of new trends of the regulatory structure for financial institutions would be the next value added step in improving regulatory coordination and oversight.



Meeting at the Federal Reserve Bank of New York



Delegation of BiH financial regulators visiting Ellis Island in New York, NY

“I have to say that it was a big privilege for us to meet with the representatives of the key financial institutions in the States who unselfishly and openly spoke not only about their experiences, their knowledge but also their mistakes”, said Ms. Slavica Injac, Director of the RS BA

“ Also, what was very important, we talked about the issues that relate to consumer protection, and all of the experiences that we heard from the counterparts in the States, we will implement to the extent possible and if applicable in our market”, said Mr. Zlatko Bars, Director of the FBA

ANNEX 6 – DCA FACT SHEET



USAID
FROM THE AMERICAN PEOPLE

BOSNIA-HERZEGOVINA

Total Portfolio Guarantee:
\$52 million

DCA Partner Banks:

- Raiffeisen Bank BiH
- Volksbank BH
- Unicredit Bank



"I would like to wish our partner banks success in using the DCA program to meet their strategic goals, expand their lending products, and help the Bosnian economy grow and thrive."

- Ambassador of the USA
at the DCA LGP Signing
Ceremony, October 2010.

Development Credit Authority (DCA) Loan Portfolio Guarantee (LPG)

Challenge

After years of commercial lending expansion, the banking sector in Bosnia and Herzegovina (BiH) is characterized by a reduction in credit growth, over liquidity and increasing requirements for credit approvals. BiH banks are still reluctant to lend to small and medium enterprises (SMEs) that do not have substantial collateral.

USAID Initiative

To address this challenge, USAID/BiH utilized the Development Credit Authority (DCA), a Loan Portfolio Guarantee (LPG) facility. The goals of DCA are two-fold: to mobilize private capital to finance development initiatives and to demonstrate the economic viability of such investments to the local banking sector. The DCA facility provides banks with a 50% guarantee on the loan principal. This enables them to make longer term loans without substantially increasing their risk exposure and to extend loans to borrowers who otherwise may not qualify for loans under the banks' regular lending parameters.

USAID/BiH's first DCA program (2003-2010) was signed with three local partner banks (Intesa Sanpaolo Bank BiH [formerly UPI Bank], Volksbank BH, and UniCredit Bank [formerly UniCredit Zagrebacka Bank]). This program provided 205 loans to private enterprises in agricultural production and processing, wood processing and tourism worth over \$30 million. The program sustained 2,832 jobs and created 601 new jobs. Enterprises that accessed financing under the DCA increased employment by 20%.

Current Activities

The second BiH DCA program was signed in September 2010 with Raiffeisen Bank BiH and Volksbank BH with combined resources of USAID and Swedish International Development Agency (Sida). This loan guarantee program in BiH is the first program under the global memorandum of understanding that USAID and Sida signed in March 2010 in Washington. This is also USAID's first-ever loan guarantee performed jointly with another donor.

This ten-year, \$40 million guarantee program is expected to strengthen local banks' ability to finance medium and long term loans to SMEs in productive sectors, and consequently increase economic growth in BiH.

In 2006, USAID signed a \$16 million DCA guarantee program with Unicredit Bank for SMEs in agriculture, wood processing and tourism. In 2010, a balance of \$12 million of loans remains that can be placed under this program until 2015.

Therefore, as of 2010, the combined resources of the current DCA programs are over \$50 million and are an important stimulus for SME development and economic growth in BiH. The DCA program is a key complement to two ongoing economic growth programs jointly funded by USAID and Sida: FIRMA and FARMA. These programs represent donor investment of over \$35 million. These programs help strengthen SMEs in agriculture, wood processing, metal processing and tourism. Another USAID project, PARE, provides administrative technical support to the DCA partner banks and DCA monitoring assistance.

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